

STATE OF ILLINOIS  
SECRETARY OF STATE  
SECURITIES DEPARTMENT

	)	
IN THE MATTER OF:	)	
	)	
MALORY INVESTMENTS, L.L.C. (CRD # 110936),	)	
RONALD STEIN (CRD # 434761),	)	
STEPHEN STRAUSS (CRD #4446296),	)	
KENNETH EUGENE ZELLMER, JR. (CRD #476238),	)	
SEAN ZARINEGAR (CRD #2244373),	)	File Number: 07-00319
(aka Bejahn Zarinegar)	)	
CAPITAL GUARDIAN, INC.,	)	
BLAKE WILLIAM WILSON (CRD #1390808),	)	
(aka Arnold Kramer,	)	
Arnold Cramer,	)	
Irv Kranberg); and	)	
CHRISTINE FENN	)	
(aka Christine Ann Gilbert),	)	
	)	
RESPONDENTS.	)	

NOTICE OF HEARING

TO THE RESPONDENTS:	Malory Investments, L.L.C. (CRD # 110936) 10937 Wilkins Avenue #304 Los Angeles, CA 90024
	Ronald Stein (CRD# 434761) 10937 Wilkins Avenue, #304 Los Angeles, CA 90024
	Stephen Strauss (CRD# 4446296) 26893 Bouquet Canyon Road, #C-410 Santa Clarita, CA 91350-3500
	Kenneth Eugene Zellmer, Jr. (CRD# 476238) 40204 N. Hickcock Trail Phoenix, AZ, 85086

Sean Zarinegar (CRD # 2244373)  
11660 Greentree Rd.  
Colorado Springs, CO 80909-4126

Capital Guardian, Inc.  
155 East El Roblar Drive  
Ojai, CA 93023

Blake William Wilson (CRD # 1390808)  
419 Tico Blvd.  
Ojai, CA. 93023

Christine Fenn  
155 East El Roblar Drive  
Ojai, CA 93023

You are hereby notified that, pursuant to Section 11.F of the Illinois Securities Law of 1953 [815 ILCS 5] (the "Act") and 14 Ill. Adm. Code 130, Subpart K (the "Rules"), a public hearing will be held at 69 West Washington Street, Suite 1220, Chicago, Illinois 60602, on the 26th day of September, 2007, at the hour of 10:00 a.m., or as soon thereafter as counsel may be heard, before James L. Kopecky, or another duly designated Hearing Officer of the Secretary of State.

This hearing will be held to determine whether an Order shall be entered which would retroactively revoke Respondent Ronald Stein's and Malory Investments, L.L.C.'s registrations in the State of Illinois, prohibit Respondents from selling or offering for sale securities in the State of Illinois, and/or grant such other relief as may be authorized under the Act including but not limited to imposition of a monetary fine in the maximum amount pursuant to Section 11.E(4) of the Act, payable within ten (10) business days of the entry of the Order.

The grounds for such proposed action are as follows:

#### **NATURE OF THE CASE**

Respondents engaged in a wide range of fraudulent securities offerings in which they conspired to sell over one hundred fraudulent offerings raising hundreds of millions of dollars. Among other acts, Respondents employed unregistered sales agents, paid undisclosed sales commissions, fraudulently overstated potential returns on investments, failed to disclose criminal

backgrounds of principals, and failed to accurately disclose use of proceeds, assets of the issuers and other material information. In fact, MALORY conducted private offerings at an average of one per week, despite MALORY operating from a residential apartment, not advertising, and not even maintaining a Yellow Pages listing.

In 1992, Blake Wilson ("WILSON") was convicted of securities fraud in the state of California. As a result of that conviction, WILSON was barred from any association with a Broker-Dealer. Despite this restriction, WILSON controlled the operation of MALORY since the inception of the firm. MALORY'S application for Broker-Dealer registration was misleading in several ways, including never disclosing WILSON'S involvement with MALORY. In fact, MALORY'S sole business and revenue came from offerings solicited and arranged by WILSON.

In order to facilitate their conduct, Respondents formed shell companies, acted under false names, used names of individuals without their knowledge, and failed to disclose the involvement of key individuals. Respondents engaged in this conduct through a Broker-Dealer that failed to maintain books and records, ignored its obligations to perform due diligence, and repeatedly filed regulatory filings containing false statements.

#### **FACTS COMMON TO ALL COUNTS**

1. From March 12, 2003 until December 18, 2006, Malory Investments, L.L.C., Central Registration Depository ("CRD") #110936, was a registered securities dealer in the state of Illinois pursuant to the Act with a current business address of 10937 Wilkins Avenue, #304, Los Angeles, CA 90024. Previous addresses for MALORY are: 6345 Balboa Blvd., Suite 259 Blg 3, Encino, CA 91316; 12966 Euclid, #150, Garden Grove, CA 92840; 1351 WestWood Blvd., #102, Los Angeles, CA 90024; and 520 S. Sepulveda Blvd., Suite 308, Los Angeles, CA 90049. CRD records indicate the authorized product types for MALORY are private placements and mutual funds.
2. RONALD STEIN ("STEIN") (CRD# 434761), is the reported "owner" (75%+ ownership) of MALORY. From March 12, 2003 until December 18, 2006, STEIN was a registered securities Salesperson in the state of Illinois. CRD records indicate that STEIN holds series 1, 40, and 63 designations. STEIN's last known residential address is 10937

Wilkins Avenue, #304 Los Angeles, CA 90024.

3. STEPHEN STRAUSS (“STRAUSS”) (CRD# 4446296), a member of MALORY, is reported to own 10% but not more than 25% of MALORY. CRD records indicate that he holds no securities designations. His recent residential addresses are 26893 Bouquet Canyon Road, #C-410, Santa Clarita, CA 91350-3500 and 8758 Saddlebrook Cove, Olive Branch, MS 38654. He has a last known business addresses of 3340 Goodman Road, South Haven, MS 38672 and 904 Rayner St., Memphis, TN 38114. Although not disclosed in any registration statement, on July 6, 1987 STRAUSS was convicted of Theft of Services 1st degree for which he was sentenced to twenty four months.
4. KENNETH EUGENE ZELLMER, JR. (“ZELLMER”) (CRD# 476238) is a principal with MALORY. His last known residential address is 40204 N. Hickcock Trail, Phoenix, AZ, 85086.
5. SEAN ZARINEGAR (AKA Bejahn Zarinegar) (“ZARINEGAR”) (CRD # 2244373), a principal of MALORY, was employed with MALORY from July 9, 2001 through April 8, 2005. His last known residential address is 11660 Greentree Rd., Colorado Springs, CO 80909-4126. He holds series 6, 7, 22, 24, 26, 39 and 63 designations. ZARINEGAR filed a personal, Chapter 7 Bankruptcy, Case #SA00-13205LR, which was discharged on July 31, 2000. The Bankruptcy involved a high-risk private investment in restaurants that resulted in major losses of personal income.
6. CAPITAL GUARDIAN INC. (“CGI”) has a business address of 155 East El Roblar Drive, Ojai, CA 93023. CGI is self-described as a third party Broker-Dealer and issuer compliance company.
7. As of December 12, 2006, CGI’s website stated that its staff includes “*a practicing attorney, a former broker-dealer, former licensed members of the NASD, an experienced*

*broker-dealer representative and other securities industry professionals with a combined experience of more than 40 years."*

8. CGI's website and documents state that it provides its clients with Broker-Dealer services regulation, compliance services (including analysis and development of compliance policies, compliance audits and draft disclosures and responses to federal and/or state document production requests), training, legal representation in enforcement actions (including complex litigation matters, regulatory investigations and proceedings, parallel criminal and civil proceedings, sales practices claims, subpoena enforcement, Cease & Desist issues, administrative hearings and other proceedings, and other claims of alleged violations), private placement disclosure document preparation, issuance of securities, blue sky registration, Broker-Dealer and agent registration, and new business formation.
9. CGI's website states that issuers *"need the experience of a broker-dealer who has been selling offerings of all types for years and has met with many obstacles."*
10. CGI's website states that *"[w]hen selling a security, whether private or public, a disclosure document is required in all cases. You are required to inform the investor of certain risks and other not-so-obvious information."*
11. BLAKE WILLIAM WILSON (AKA Arnold Kramer, Arnold Cramer, and Irv Kranberg) (CRD # 1390808) is the owner of CGI. He has a last known business address of 155 East El Roblar Drive, Ojai, CA 93023 and a last known home address of 419 Tico Blvd., Ojai, CA. 93023. From July 17, 1985 to August 14, 1992, WILSON owned and operated NASD Broker-Dealer Blasanne, Inc. (CRD # 16647), aka: Blago Oil Company.
12. On November 11, 1992, WILSON was convicted of a felony, to wit: "False Statement to Sell Securities" in the state of California. As a result of that conviction, WILSON was

barred by California from association in the securities industry, to wit: “position of employment, management, and control of any Broker-Dealer and/or Investment Adviser.”

13. On June 29, 1992, the NASD censured and barred WILSON from association with any member of the NASD in any capacity for violation of Rules of Fair Practice, to wit: “WILSON failed to respond to NASD request for information made pursuant to Article IV, Section 5 of the Rules of Fair Practice concerning an investigation of his securities business.”
14. Although not disclosed as a principal of MALORY, WILSON controlled MALORY. He exercised the ability to recruit, hire and register Salespeople. He also was the only person who solicited and negotiated with issuers and had the ability to commit MALORY to act as the Broker-Dealer of Record. The only source of income for MALORY came from the WILSON negotiated deals.
15. CHRISTINE FENN (aka Christine Ann Gilbert) (“FENN”) is an employee of CGI and is the administrator/administrative assistant for MALORY. She has a last known business address of 155 East El Roblar Drive, Ojai, CA 93023.
16. A review of the files of the Illinois Securities Department did not disclose any record of the registrations of Respondents CGI AND WILSON as either a Broker-Dealer and/or Salesperson in the state of Illinois. In fact, if WILSON attempted to register as such, his prior criminal conviction for securities fraud would act as a disqualification. Although MALORY listed FENN as an Administrative Assistant on at least one MALORY filing, FENN was not registered with the Illinois Securities Department in any capacity.

#### **MALORY AUDIT**

17. On October 23, October 24, and October 26, 2006, examiners from the California Department of Corporations, the Office of the Kansas Securities Commissioner and the

Pennsylvania Securities Commission conducted an audit of the books and records of MALORY.

18. As of July of 2006, the main office address of MALORY disclosed on the CRD was 520 S. Sepulveda Boulevard, Suite 308, Los Angeles, CA 90049.
19. According to California Department of Corporations records, 520 S. Sepulveda Boulevard, Suite 308, Los Angeles, CA 90049 is the business address of Andrick Financial Securities Inc. and Andrick Securities. According to the owner of the Andrick firms, MALORY never occupied an office at that location, and no records for MALORY were ever kept at that location.
20. The books and records of MALORY were located at 10937 Wilkins Avenue #304, Los Angeles, CA, 90024, which is located in a restricted access apartment building and is the residential address of STEIN and his wife.
21. During the October audit of MALORY, examiners located a Written Supervisory Procedure manual ("WSP") dated July 27, 2001. The document appeared to be generic in form and had been downloaded from the Internet. The document had been trademarked *Books on Screen*, and appears to have been published by Compliance International, Inc. No updates have been made to the WSP since July 2001. The WSP did not contain Anti-Money Laundering procedures.
22. Sections 5.2 through 5.3.1 of the WSP established guidelines for the drafting, approval and retention of incoming and outgoing correspondence. STEIN was designated as the responsible party for approving and retaining all correspondence. MALORY and STEIN failed to maintain incoming and outgoing correspondence for the firm and its registered representatives.

23. The examiners found that MALORY and its employees did not maintain client files. STEIN stated that his firm did not sell any PPO's ("Private Placement Offerings") and only sold one mutual fund since the inception of the firm.
24. STEIN stated that MALORY received no commission on any sales of PPO's for which the firm was the Broker-Dealer of record.
25. During the audit, STEIN stated that MALORY received \$2,000 per PPO for which it was the Broker-Dealer of record. STEIN stated that he never spoke to the issuer of a PPO. STEIN further stated that CGI, acting by and through FENN and WILSON, negotiated the Broker-Dealer agreement for MALORY with respect to these PPO's.
26. During the audit, the examiners found one hundred and seven private placement memoranda ("PPM's") for which MALORY was the Broker-Dealer of record. STEIN stated that since the inception of the firm in 2002, no MALORY agent had ever sold a PPO.
27. Section 16.1.2.1 of MALORY'S WSP states that (Section 4(2) of the Securities Act of 1933) states:
- "Some private placements are offered under section 4(2) which provides an exemption for 'transactions by an issuer not involving any public offering.' While the section does not specifically outline the requirements for establishing an exemption, the following is a summary of requirements gleaned from SEC interpretations and court decisions.*
- There may be no general solicitation of purchasers.*
- Offerees and purchasers must have access to information about the issuer and must be able to comprehend and evaluate the information.*
- The issuer, broker-dealer and others acting for the issuer must conduct due diligence to reasonably insure the information given to Offerees and purchasers is complete and accurate.*
28. During the examination, STEIN gave inconsistent statements to examiners regarding due diligence investigations of offerings for which MALORY was shown as Broker-Dealer of



record. Initially, he stated that he, as principal of MALORY, performed due diligence on each private placement. Later, when no due diligence information was located on the PPM's or for the issuers of the offerings, STEIN stated that MALORY relied on CGI to conduct due diligence investigations.

29. WILSON'S involvement, felony conviction, and bar from association with Broker-Dealers was never disclosed to investors by any of the PPO's reviewed for which MALORY was the Broker-Dealer of record and for which CGI performed due diligence, subscription tracking services, PPM preparation and other services.
30. Section 2.21.4 of the MALORY's WSP requires that a background investigation be conducted on all new employees. STEIN stated that neither STRAUSS, ZELLMER, ZARINEGAR, nor he ever interviewed the MALORY agents prior to hiring them and never conducted a background investigation on them. STEIN further stated that he was informed by WILSON which agent was to be registered with MALORY. STEIN stated that on at least two occasions, WILSON instructed STEIN to allow two agents to park their license with MALORY. STEIN stated that he followed WILSON'S orders, hiring Michael Jones (CRD # 2157872) on August 26, 2004 and Jeremy Dane Jobe ("JOBE") (CRD #4271958) on June 6, 2006.
31. Jobe (CRD #4271958) was hired by MALORY on June 6, 2006 as a registered representative, despite the fact that on February 28, 2006, Jobe was issued a summary Order to Cease and Desist (2006-02-06) by the Pennsylvania Securities Commission regarding an offering named 504 Fund Inc.
32. Sections 2.21.5 and 4.0 of the WSP identified STEIN as the designated principal on regulatory filings, requiring STEIN to make all regulatory filings for MALORY and its employees, including U-4 filings and fingerprints. In reality, FENN and CGI made all filings for MALORY with little or no review by STEIN.

33. On July 6, 1987, STRAUSS was convicted of Theft of Services 1<sup>st</sup> degree for which he was sentenced to 24 months. Respondents failed to disclose the criminal record of STRAUSS on the CRD. On March 25, 2002, the California Department of Corporations issued a Desist and Refrain Order for the sale of unregistered securities issued by Stovact, Inc. to STRAUSS, who at the time was the Director of Business Affairs for Stovact, Inc. The CRD records indicate that STRAUSS was the Chief Operating Officer of Stovact Inc. STRAUSS, STEIN, FENN, and MALORY failed to disclose this Desist and Refrain Order on STRAUSS' U-4.
34. Since its inception, MALORY has employed fifty-five registered agent. MALORY maintained incomplete personal files for those agents. When asked to produce information on all its employees, MALORY produced partial information on only forty-six agents.
35. FENN signed as the administrator on many documents that were printed on MALORY letterhead. FENN conducted numerous activities on behalf of MALORY, CGI and the issuers, including filing the registrations of Broker-Dealers for MALORY and making notice filings for the issuers.
36. In a document dated September 4, 2002, FENN sent a letter to NASD Registration, Inc., regarding the "Broker Dealer Initial Registration Fees and Agent Registration Fees" for registration in 40 states.
37. During the audit, an examiner located an e-mail from FENN (From: Christine<Christine@west.net>) to STEIN (To: Ronald Stein < maloryllc @ hotmail.com >) dated September 21, 2006. In the e-mail, FENN writes:

*"I spoke to the woman listed on the letter from the NASD in regards to Jobe. She said she had posted the waiver, however, it was pending due to the fact that there is still disclosure issue. When you have a chance, can you tell me what they are? I also spoke to Rob and he wanted to know if I had sent off the fingerprints and fee's to the NASD. I told him I was waiting for the SEC matter to be sent through. He asked if you were o.k. with*

*the U-4's that have been sent to you, especially Kirk Smith. I suppose we will need to collect an additional \$95.00 disclosure fee for the NASD as well as for Amato (I am sending to you today) with a check for \$500. Thanks, Christine"*

38. Section 11.3 of the WSP (Branch Offices Assigned to the Office of Supervisory Jurisdiction) ("OSJ") states:

*"Each branch office that is not an OSJ will be assigned to the supervision of an OSJ. The designated supervisor is required to visit non-OSJ branch offices on a periodic basis and record the visit in a memorandum or other record to be retained by the designated supervisor for the branch location.*

39. Section 11.4 of the WSP (Non-Branch Business Location) states:

*"Visit the non-branch location at least quarterly or require the RR(s) to visit the OSJ at least quarterly... Document visits to non-branches and /or meetings with non-branch RR(s)."*

40. STEIN stated that he did not conduct internal audits or visits as is required in the firm's WSP cited in paragraphs 38 and 39.

41. STEIN stated that MALORY delegates compliance responsibilities to CGI. These compliance activities include but are not limited to registration filings for the firm and its agents, due diligence for all offerings, hiring of agents, training of agents, registration of agents, scheduling for exams, and assistance to STEIN in written responses to state regulators as well as the NASD and the SEC.

42. STEIN stated that WILSON and CGI marketed MALORY'S services to the issuers. STEIN further stated that the only sources of revenue for MALORY were the Broker-Dealer agreements with issuers that were brought to MALORY by WILSON and CGI.

43. In an e-mail dated December 8, 2004 (7:42 PM) from Monty Mayfield (MrNewBiz@aol.com) to CGI (cgi@west.net), Mr. Mayfield requested information on CGI's services and costs associated with those services. He identified himself as a person who has "an interest in raising money on oil and gas investments/projects..."

44. In response to Mr. Mayfield (MrNewBiz@aol.com), on December 9, 2004 (9:39 AM), FENN (cgi@west.net) outlined the services provided by CGI and the cost of each service. The e-mail reads as follows:

*"Dear Mr. Mayfield, thank you for contacting us. We are a full service compliance company as our website states. For a 506 PPM, a 25102 (n) California PPM (if applicable), SEC filing of the Form D, our fee's are \$18,000. Blue sky doc's and fee's are mandatory in each state where there is an investor. We strongly recommend using a Broker dealer to underwrite the project. We can recommend. There is a \$2,000 fee paid directly to the BD. We also do all the clearing and tracking, verify if investor is accredited or not, send out certificate and keep you posted on keeping your non-accreds under 35. State blue sky fee's are \$1,350 per state (including state fees). California (if 25102(n) and NY are \$2,350.....Thank you. Christine Fenn"*

45. In an e-mail dated December 9, 2004 (2:23 PM) from "E A" (MrNewBiz@aol.com) to CGI (cgi@west.net), "E A" (identity unknown) wrote:

*"One of my 'partners' was also impressed about what I shared with him about your company and financial requirements, BUT he had one question: re the Broker/Dealer, the fee is \$2k, but are there any additional fees or points due the BD? Thanks."*

46. In response FENN (cgi@west.net) writes on December 9, 2004 (3:54 PM) the following:

*"Yes, 6.5% on monies invested. Example Joe Smith invests \$10,000, 6.5% of that is \$650. In addition, if you have employees that are to receive commission, they need in state to have a series 63 license and out of state a 7. They then would hang their license with a BD and work out a commission structure together. I have training contacts if you need them for the series 63 and 7. Thank you. Christine."*

### **CAPITAL GUARDIAN**

47. CGI, WILSON and FENN drafted and/or filed the PPM and/or allegedly conducted subscription tracking for at least one hundred and seven offerings for which MALORY was Broker-Dealer of record. In some but not all offerings, CGI is noted as providing subscription tracking services.
48. CGI charged some issuers a commission of as much as 6.5%. CGI attempted to disguise these commissions as "subscription tracking fees" or "clearing fees."

49. On or around February 6, 2004, a letter between employees of Coomer Energy, Inc. detailed their understanding of what the fee structure was for Capital Guardian. That letter stated that the fees were as follows:
- “\$20,000 to \$30,000 – Capital Guardian  
\$15,000 to \$20,000 – State registration and filing  
\$2,000 to \$3,000 – Broker-Dealer + 6 ½ % of each sale/ so that’s  
\$65,000 or more”
50. On or around September 14, 2005, CGI received a check from another issuer, Kentucky Mountain View Petroleum, Inc. The payee on the check was “Mallory Investments or Capital Guardl” [sic] with a memo on the check indicating that there was a “3.5% broker-dealer agreement.” The check was deposited in a CGI bank account at Washington Mutual Bank, FA.
51. WILSON negotiated with the issuers for all services provided by CGI and MALORY, including but not limited to Broker-Dealer services regulation, compliance services (including analysis and development of compliance policies, compliance audits, drafting of disclosures, and responses to federal and/or state document production requests), training, legal representation in enforcement actions (including complex litigation matters, regulatory investigations and proceedings, parallel criminal and civil proceedings, sales practices claims, subpoena enforcement, Cease & Desist issues, administrative hearings and other proceedings, and other claims of alleged violations), preparation of private placement disclosure documents, issuance of securities, blue sky registration, Broker-Dealer and agent registration, and new business formation.
52. The offering materials for issuers in which MALORY was the Broker-Dealer of record failed to disclose: (1) any involvement by WILSON and (2) WILSON's 1992 conviction of securities fraud in the state of California.

53. Respondent STEIN told examiners that records of MALORY were being kept at CGI. However, during a visit to CGI conducted in order to retrieve MALORY records, an examiner heard FENN tell STEIN on a phone conversation that the records STEIN wanted CGI to release to examiners did not belong to STEIN or to MALORY but instead belonged to CGI and the issuers. Despite requests made to WILSON by both the examiners and STEIN and a California Department of Corporation's order to produce the due diligence records, those records were never produced. In fact, CGI represented to examiners that no due diligence files existed because CGI did not conduct due diligence examinations.
54. In addition to the due diligence records, the State of California requested pursuant to a Judicial Order that CGI immediately produce for review, inspection and copying by the California Corporations Commissioner (or designee(s) of the Commissioner) all books, papers, correspondence, memoranda, agreements, or other documents or records relating to MALORY, or any issuer for which MALORY was listed as the Broker-Dealer, including any books, papers, correspondence, memoranda, agreements, or other documents maintained in electronic format of any type.
55. As of September 23, 2005, the CGI website provided the viewer with a selection that stated "CLICK HERE for a list of regulators and other persons working with various state securities agencies." Once the viewer clicked on the selection, a second page was revealed that stated "Please Call Us @ (805)646-4656 or Email Us For A Current List Of Persons Posing As Investors."
56. The examiners received a document from CGI containing a list of the undercover names and/or names of regulators for eleven states and the FBI that purportedly posed as potential investors.
57. On September 12, 2000, the Wisconsin Department of Financial Institutions issued an Order of Prohibition and Revocation against BLAKE W. WILSON aka: Arnold Kramer,

aka: Arnold Cramer and aka: Irv Kranberg. The Order states that WILSON, “aka Arnold Kramer, aka Arnold Cramer, aka Irv Kranberg, his agents, servants, employees, and every entity and person directly or indirectly controlled or organized by or on his behalf, are prohibited from making or causing to be made to any person or entity in Wisconsin any further offers or sales of securities unless and until such securities are registered.”

58. The petition for the Wisconsin Order cited that WILSON was the controlling person of issuers Sierra West Unit Investment Trust, Sierra West-A Unit Investment Trust, and Pac West II Unit Investment Trust.
59. The petition for the Wisconsin Order further recited that during 1997 WILSON used unlicensed agents to sell securities issued by the entities listed in paragraph 58 above to Wisconsin residents.
60. The petition for the Wisconsin Order further stated that the securities sold as exempt securities under Reg. D Rule 506 were not exempt from registration because they had been sold to non-accredited members of the general public.
61. The the Illinois Securities Department is in receipt of information that Respondents MALORY, STEIN, STRAUSS, ZELLMER, ZARINEGAR, CGI, WILSON, AND FENN engaged in the offer and/or sale of securities to Illinois residents, that were neither registered nor exempt from registration in the state of Illinois.

#### **PRIVATE PLACEMENTS AND ISSUERS**

62. MALORY was listed as the Broker-Dealer of record on at least sixty-four offerings which were purported to be exempt from federal and state registration under Reg. D. Most of the offerings were either fraudulent and/or violated the Reg. D exemption requirements.

Mercer Capital Inc., Mercer Capital Management Inc., Tri-State Energy Group LLC, Tri-State Energy Group I, LTD., Tri-State Energy Group I, LP and Tri-State Energy Group II, LTD.

63. MALORY is listed as the Broker-Dealer of record on a copy of a signed Securities and Exchange Commission (“SEC”) Reg. D 506 filing for a securities offering by Tri-State Energy Group I, LP found by the examiners at the offices of CGI.
64. On May 3, 2006, Mercer Capital Management, Inc., issued a check to CGI for \$2,000. The notation in the check’s memo line was “Tri-State.” The check was deposited in a CGI bank account located at Washington Mutual Bank, FA.
65. MALORY signed a Broker-Dealer agreement with Tri-State Energy Company for an offering by Tri-State Energy Group II, Ltd. STEIN and Robert L. Flickinger, II (“Flickinger”), the principal of Mercer Capital Management, Inc., and Vice-President of Tri-State Energy Company LLC, signed the Broker-Dealer agreement.
66. On July 25, 2006, Mercer Capital Management, Inc., issued a check to MALORY for \$2,000. The notation in the memo line was “Tri-State II.”
67. The Tri-State Energy Group II, Ltd. private placement memorandum states that the “General Partner has contracted services for the compliance to securities laws relative to the sale and solicitation of the Limited Partnership Units. These securities “compliance services” may include, but are not limited to, Blue Sky and Private Placement Memorandum preparation and filing.” This memorandum states that the compliance company is to be paid 5% of the offering (\$2,000,000). CGI was contracted as the “compliance service” provider.
68. The PPM referred to in Paragraph 67 failed to name CGI as the compliance service provider and failed to disclose WILSON’s criminal record and administrative sanction.



69. The Tri-State Energy Group II, Ltd. private placement memorandum states that Flickinger has served as the Vice-President of Tri-State Energy Company LLC since December of 1999.
70. On November 22, 2006, the SEC, in conjunction with the National Futures Association, brought an emergency action against Mercer Capital Inc., Mercer Capital Management, Inc., Tri-State Energy Group LLC, Tri-State Energy Group I, LTD., Tri-State Energy Group II, LTD, and Flickinger.
71. In the complaint which supported the emergency action, the SEC alleged that Mercer Capital Inc., Mercer Capital Management, Inc., Tri-State Energy Group LLC, Tri-State Energy Group I, LTD., Tri-State Energy Group II, LTD, and Flickinger were engaged in the fraudulent trading of securities issued by Tri-State Energy Company LLC, a Casper, Wyoming company.
72. Due to MALORY'S and CGI's failures to conduct due diligence on the issuers referred to in Paragraph 70 and the issuer-provided information for the PPM's used in their offerings, the investors were deprived of the opportunity to learn of the fraud relating to these offerings.
73. Kirk Devon Smith (CRD #1002884) was hired by MALORY on October 9, 2006. He is also employed by Mercer Capital Inc., a commodities dealer located in Portland, Oregon. STEIN did not conduct a pre-employment interview with Smith and did not conduct an inquiry after the SEC's action against Mercer Capital, Inc., referred to in Paragraphs 69 and 70. Acting through CGI, WILSON took actions, including the payment of registration fees, in order to obtain Smith's registration as an agent with MALORY.

North American Resource Group

74. Beginning in December 2005 and continuing to March of 2006, MALORY hired at least fourteen agents who had previously been employed by North American Resource Group ("NARG"). A review of CGI records revealed that NARG paid CGI for the NASD registration fees for the NARG agents that were hired by MALORY. A fax cover sheet dated June 19, 2006 from STEIN to FENN discussed the increased premium for MALORY fidelity bond renewal. It states that "NARG is causing a large increase in the premium. I believe NARG should pay for the increase." A letter from Candace D. Shirley of NARG to FENN states, "I am enclosing a check in the amount of \$294 payable to Malory Investments, LLC for the fidelity bond renewal."
75. On December 8, 2005, NARG drafted a check (#9243) in the amount of \$6,300.00 to the NASD. The description on the corresponding check stub reads "Legal and Professional Expense."
76. On December 12, 2005, NARG drafted a check (#9247) in the amount of \$3,490.00 to the NASD. The description on the corresponding check stub reads "Legal and Professional Expense."
77. On December 12, 2005, STEIN wrote a letter to the NASD CRD-IARD regarding the renewal of MALORY's registration. In the letter, STEIN references two checks in the amount of \$6,300.00 and \$3,490.00. "Enclosed are two checks for \$6300.00 and \$3,490.00 toward my 2006 renewal. If you have any questions, please [call] give Christine [FENN], my administrator on my account."
78. On March 22, 2006, the Alabama Securities Commission issued a Cease and Desist order to NARG and several of its principals related to the offer and sale on an unregistered security.

79. Despite the dual employment of agents by MALORY and NARG, MALORY failed to conduct any review of the activities of the NARG employees following the Alabama Cease and Desist order.

LifeLine Imaging LLC

80. Lifeline Imaging is a California Limited Liability Company and is owned and operated by Randy Morton ("Morton"). Since 2001, LifeLine has sold securities in at least 8 separate offerings that LifeLine claimed to be exempt from securities registration. In connection with these offerings, Lifeline filed Form D's which it had reason to know would be available to the investing public. MALORY was the Broker-Dealer of record on at least three (3) LifeLine Imaging Reg D 506 filings with the SEC and with the states.<sup>1</sup>
81. MALORY hired at least four former sales employees of Pacific Network and Consulting. Pacific Network and Consulting was the call center that marketed only the Lifeline Imaging PPO's.
82. CGI, WILSON, and FENN took all actions to register the representatives referred to in Paragraph 80 as MALORY agents.
83. CGI drafted and/or filed each of the PPM's on behalf of Lifeline securities offerings. CGI, WILSON, FENN, and Morton failed to disclose on these PPM's Morton's felony convictions for transporting narcotics and possession of a controlled substance/narcotics.
84. The state Notice filings and/or federal Form D filings for LifeLine Imaging of Los Gatos, Advanced Health Care Group of Dallas, and Advanced Imaging-Ft. Worth, issued by companies owned and controlled by Morton, indicates that MALORY was the Broker-Dealer of Record on these securities offerings. However, it was never disclosed in those offerings that Morton negotiated the offerings only with WILSON, an individual who was

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<sup>1</sup> LifeLine Imaging of Los Gatos, Advanced Health Care Group of Dallas, and Advanced ImagingFt. Worth.

not registered with MALORY, and who was prohibited from any association with a Broker-Dealer.

85. In a statement made by Daniel Alfred Caterino (“Caterino”) to examiners, Caterino stated that he was merely a consultant for LifeLine. However, Caterino maintained an office located at Pacific Network and Consulting’s office address. Caterino has a criminal record that includes drug-related charges, burglary, theft, and grand theft auto.
86. On October 17, 2000, Caterino and seven other respondents were named in a Wisconsin Order of Revocation of Exemption finding that Respondents committed fraud in the offers and sales of unregistered securities by an unlicensed Broker-Dealer and Salesperson. The issuer of those securities was Heart Scan, LLC. Caterino was named as an agent for the unlicensed Broker-Dealer, Cornerstone Financial (aka: Pacific Capital Network).
87. In a statement taken from Ken Perdue (“Perdue”) by the examiners, Perdue stated that he assisted in the management and the operation of Pacific Network and Consulting and that Pacific Network and Consulting utilized unregistered Salespersons. Perdue stated that the unregistered Salespeople “cold called” potential investors throughout the United States. The initial call would be made by a “fronter”, and if the potential investor was interested, the investor would be transferred to a “closer”. In the event of a sale, both the fronter and the closer would receive a commission. Perdue stated that if the issuer wanted to raise \$1,000,000 for working capital, the offering would be for \$2,000,000 because the cost of raising the funds would be approximately 50% of the total offering amount.
88. Perdue stated that Caterino operated and supervised Pacific Network and Consulting. Furthermore, additional former Pacific Network and Consulting employees verified that Caterino managed, operated and supervised the call center’s operation. At least 80 of the

agents of Pacific Network and Consulting were not registered at the time they sold the offerings for LifeLine.

89. WILSON came to the call center on several occasions and met with Caterino.
90. WILSON and FENN, acting on behalf of MALORY, hired and registered at least four Pacific Network and Consulting Salespeople.
91. One of the Salespeople hired by WILSON and FENN was Thomas Glinskas, (CRD # 4618972). In a statement by Glinskas taken by the examiners, Glinskas said he had never heard of STEIN. He stated that WILSON arranged for him to take the NASD Series 22 classes at the LifeLine call center and to become registered with the NASD through a sponsoring company. Glinskas said that he did not know who the sponsoring company was. Glinskas stated that WILSON was present at the Pacific Network and Consulting call center on multiple occasions.
92. Perdue has arrests or criminal convictions for violations of securities laws, unlawful sale of securities, offer or sale of unqualified securities, selling false securities, counterfeiting checks, grand theft, conspiracy, theft of government property, embezzlement, false statements (2 counts), damage to property, and DUI.
93. On February 2, 2005, the Alabama Securities Commission issued a Cease and Desist Order (CD-2005-0004) against LifeLine Imaging, LLC.
94. On June 3, 2003, the Kansas Office of the Securities Commissioner issued a Cease and Desist Order (2002-4477) against LifeLine Imaging, LLC.
95. On January 28, 2003, the State of Missouri issued a Stipulation and Consent Order (#AO-03-02) against LifeLine Imaging, LLC.

96. On October 1, 2003, the California Department of Corporations issued a Desist and Refrain Order against LifeLine Imaging Systems, Inc.
97. On June 3, 2005, the State of Nebraska issued a Cease and Desist Order against LifeLine Imaging, LLC.
98. On February 26, 2003, the State of Pennsylvania issued a Cease and Desist Order (2003-02-32) against LifeLine Imaging of Long Beach Unit Investment Partnership, which is an offering made by issuer LifeLine Imaging, Inc.
99. In August of 2005, Morton resigned and appointed Stanley Johnson, who formerly acted as an unregistered Salesperson of Pacific Network and Consulting, as the general partner of LifeLine Imaging and the issuers of the other offerings made by Morton. The only assets of Lifeline at that time were leases on two buildings in Laguna Hills, California and Ft. Worth, Texas.
100. Stanley Johnson ("Johnson"), an admitted closer for the LifeLine offerings, stated that while he was an unregistered Salesperson for Pacific Network and Consulting, "fronters" were paid on an hourly rate plus a 2% commission if a sale was made from one of their contacts. He further stated that the closers received an 18% commission on each sale. Johnson said that each manager received an additional 2 to 3% from each sale.
101. In addition to other fees received, CGI received 6.5% of each investment as a commission disguised as "subscription tracking." Checks made payable to CGI from issuer LifeLine Imaging LLC ("Lifeline"), located in Orange County, CA, reflect "6.5%" in the memo line. CGI was retained to write the offerings, file the necessary "blue sky" filings, perform subscription tracking services for LifeLine, and send the investors a "Welcome Aboard" letter. CGI recommended that MALORY be used as the Broker-Dealer of record for the LifeLine offerings. CGI billed LifeLine for a Broker-Dealer fee and issued

a check to MALORY for Broker-Dealer fees for the Advance Imaging – Ft. Worth LP offering.

102. The LifeLine PPM's failed to disclose that CGI was the compliance service/tracking service and failed to disclose WILSON's criminal record and administrative sanctions. They also failed to disclose the commissions paid to CGI, which were described as "subscription tracking fees."
103. An analysis of the bank accounts for LifeLine revealed that investors' funds from the offerings were co-mingled. The co-mingling of funds makes the identifying, measuring, interpreting or recording of the economic results of the separate LifeLine offerings inaccurate.

Consulting Dynamics Inc./Advance Body Imaging, LP

104. Consulting Dynamics, Inc., is a Nevada corporation with a business address of 1339 Katella Orange, CA. Stanley Johnson is the general partner and chief operating officer. Advance Body Imaging, LP is a California limited partnership formed by Consulting Dynamics for the purpose of funding the construction of medical imaging centers.
105. The Form D filing by Advance Body Imaging, LP, dated July 13, 2004, indicated that MALORY was the Broker-Dealer of Record. However, in regards to MALORY's participation as the Broker-Dealer, the offering never disclosed that Stanley Johnson negotiated only with WILSON, an individual not registered with MALORY, and prohibited from any association with a Broker-Dealer.
106. Johnson admitted to the examiners that he operated a call center utilizing unregistered sales agents to sell the PPO for Advance Body Imaging, LP. The PPM for that offering failed to disclose these unregistered Salespeople.

107. Johnson met WILSON while Johnson was working as an unregistered Salesperson for LifeLine Imaging.
108. Johnson stated to examiners that WILSON and CGI wrote the PPM and filed the Form D and notice filings for Advance Body Imaging, LP.
109. On July 7, 2004, Consulting Dynamics issued a check to CGI for \$1,800.00. The memo line indicated that it was a payment for “broker dealer fees.”
110. On September 29, 2004, Consulting Dynamics issued a check to CGI for \$2,000.00. The memo line indicated that it was a “broker dealer” payment.
111. At least one sales agent for Consulting Dynamics was a registered Salesperson of MALORY at the time he received commission checks from Consulting Dynamics.
112. On July 21, 2006, the Alabama Securities Commission issued a Cease and Desist Order against Consulting Dynamics, Advance Body Imaging, Stanley Johnson, and other officers for the sale of unregistered securities by unregistered Salespeople.
113. An analysis of the bank accounts for Consulting Dynamics revealed that the investors’ funds were deposited in both the general partner’s account and the issuer’s account and were repeatedly transferred between accounts.

The Loan Shoppe, Inc.

114. The Loan Shoppe, Inc. is an Alabama corporation that had mailing addresses of 3183 East Pelham Parkway, Pelham, Alabama, and 777 South State Road 7, Margate, Florida. The owner and operator of The Loan Shoppe is Charles Carver. WILSON negotiated with Charles Carver of The Loan Shoppe to provide Broker-Dealer services for The Loan Shoppe, Inc.’s corporate bond offering. In a June 8, 2004 letter written by J. B.



Grossman, attorney for The Loan Shoppe and Carver, Grossman acknowledges the Broker-Dealer agreement between CGI and The Loan Shoppe in which CGI was to receive 4.5% of the capital raised through the offering. He also questioned CGI's lack of NASD registration as a Broker-Dealer.

115. In a May 26, 2004, State of New York publication of *Securities Offerings*, MALORY is cited as the Broker-Dealer of record for The Loan Shoppe offering of Corporate Bonds. However, a Broker-Dealer agreement between MALORY and The Loan Shoppe has not been located.
116. On December 12, 1991, Charles Carver was arrested and subsequently convicted for felony Possession of a Controlled Substance. The Loan Shoppe's PPM did not disclose Charles Carver's felony conviction.
117. On August 23, 2004, the Alabama Securities Commission issued a Cease and Desist Order against The Loan Shoppe, Inc. and Charles Carver as result of the offer and sale of unregistered securities, in the form of promissory notes, to investors. Despite this Alabama Order, Respondents failed to conduct any review of their involvement in the Loan Shoppe offering.
118. In October 2006, the principals of The Loan Shoppe, Charles Carver and Mario Robert Naranjo, were indicted by a Federal Grand Jury in the Southern District of Florida for criminal activity related to the sale of securities issued by The Loan Shoppe, including wire fraud, mail fraud and money laundering.

#### Amerivet Securities

119. In an offering named Phase Two Value Creating Fund, CGI and MALORY used the name of Elton Johnson in the offering as the fund manager. Johnson's signature appeared on a MALORY Broker-Dealer agreement that was also signed by STEIN. Mr. Johnson,

who is a reservist with the military, stated that he was deployed overseas on the date the agreement was signed. He further stated he did not give anyone permission to use his name in the Phase Two offering or to sign his name to any documents.

120. The principal of Phase Two Value Creating Fund is Michael Andre Jones (CRD # 2157872). He was employed by MALORY from August 26, 2004 to June 9, 2006. Jones is also a former employee of Amerivet Securities (CRD # 34786), an NASD registered Broker-Dealer, which is owned by Elton Johnson.
121. On June 26, 2006, three complainants filed an NASD Dispute Resolution Arbitration (06-02978) against Michael Jones for misrepresentations made during the sale of “pre IPOs.” The sale took place on May 18, 2006 while Michael Jones was a registered agent of MALORY.
122. Prior to WILSON forming MALORY, Amerivet Securities was used as the Broker-Dealer of record for offerings conducted by CGI. According to Elton Johnson, WILSON paid Johnson a flat fee of \$400.00 to use Amerivet’s name in regulatory filings related to the offerings. Elton Johnson stated that WILSON told him that no Salespeople were needed because the sales would be made by other unidentified individuals. According to Johnson, Amerivet agents never made any sales of offerings brought by WILSON.
123. Elton Johnson stated that he had known both WILSON and STEIN from the “chop shops” (boiler rooms) that were located in the Los Angeles, California area.

#### **VIOLATIONS OF THE ILLINOIS SECURITIES ACT**

124. Section 12.F of the Act provides that it shall be a violation of the Act for any person to engage in any transaction, practice or course of business in connection with the sale or purchase of securities which works or tends to work a fraud or deceit upon the purchaser or seller thereof. Respondents violated Section 12.F of the Act, in that:

- A. Respondents allowed WILSON to act as an undisclosed principal of MALORY, despite the fact that as a result of his earlier securities fraud conviction WILSON was barred from any association with a Broker/Dealer.
- B. Respondents failed to disclose prior criminal and regulatory actions against the principals of MALORY.
- C. Respondents represented to investors that the securities of MALORY's underwriting clients were exempt from registration, while in fact Respondents knew, or should have known, that the securities were being sold in a manner inconsistent with claimed exemptions.
- D. Respondents circulated private placement memoranda knowing or having reasonable grounds to know that the memoranda contained false or untrue material representations.
- E. Respondents failed to disclose to investors that CGI was the firm providing "subscription tracking services" and that CGI was operated by WILSON, a person with a prior conviction for securities fraud.
- F. Respondents participated in the offer and sale of Lifeline Imaging securities while the Respondents knew, or should have known, that the criminal background of officers of Lifeline was not disclosed to investors.
- G. Respondents participated in the offer and sale of Lifeline Imaging securities while the Respondents knew, or should have known, that unregistered Salespeople were selling the securities.
- H. Respondents participated in the offer and sale of the securities issued by Advance Body Imaging, LP while the Respondents knew, or should have known, that the proceeds of the offerings were being co-mingled with those of the accounts of the general partner.
- I. Respondents participated in the offer and sale of Advance Body Imaging, LP securities while the Respondents knew, or should have known, that unregistered salespeople were selling the securities.
- J. Respondents participated in the offer and sale of securities issued by The Loan Shoppe, while the Respondents knew, or should have known, that the criminal background of the Loan Shoppe's owner and operator was not disclosed to investors.
- K. Respondents participated in the offer and sale of securities issued by Phase Two Value Creating Fund while the Respondents knew, or should have

known, that the fund used the name of the proposed fund manager without his knowledge or consent.

- L. Respondents participated in the offer and sale of securities issued by Phase Two Value Creating Fund, while the Respondents knew, or should have known, that the proposed fund manager for the fund was deployed overseas.
- M. Respondent CGI held itself out as a Broker-Dealer and acted as a Broker-Dealer, while not registered as such.

125. Section 12.G of the Act provides that it shall be a violation of the Act for any person to obtain money or property through the sale of securities by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances in which they were made, not misleading. Respondents violated Section 12.G of the Act, in that:

- A. Respondents received money from the sale of securities issued by MALORY'S underwriting clients without disclosing the involvement of WILSON and his prior criminal conviction.
- B. Respondents received money from the sale of securities issued by MALORY'S underwriting clients, claiming the securities were exempt from registration, while in fact Respondents knew, or should have known, that the securities were being sold in a manner inconsistent with claimed exemptions.
- C. Respondents received money from the sale of securities issued by MALORY'S underwriting clients, knowing or having reasonable grounds to know that private placement memorandums used to market the securities contained false representations.
- D. Respondents received money from the sale of securities issued by Lifeline Imaging while the Respondents knew, or should have known, that the criminal backgrounds of Lifeline officers were not disclosed to investors.
- E. Respondents received money from the sale of securities issued by The Loan Shoppe while the Respondents knew, or should have known, that the criminal background of owner and operator of the Loan Shoppe was not disclosed to investors.
- F. Respondents received money from the sale of securities issued by Consulting Dynamics Inc. and securities issued by Advance Body Imaging, LP while the Respondents knew, or should have known, that Consulting Dynamics Inc.

and Advance Body Imaging, LP failed to disclose that the proceeds of the offerings were being commingled.

- G. Respondents received money from the sale of securities issued by Phase Two Value Creating Fund while the Respondents knew, or should have known, that the person named as the fund manager was not associated with the offering.
- H. Respondents CGI, WILSON and FENN received money in connection with the sale of securities by falsely holding CGI out as a Broker-Daler while it was not registered as such.

126. Section 12.E of the Act states, *inter alia*, that it shall be a violation of the provisions of the Act for any person to make, or cause to be made, in any application, report or document filed under the Act or any rule or regulation made by the Secretary of State pursuant to the Act, any statement which was false or misleading with respect to any material fact. Respondents violated Section 12.E of the Act, in that:

- A. Respondents MALORY, STEIN, STRAUSS, ZELLMER, ZARINEGAR, CGI, WILSON, and FENN filed a false Broker-Dealer application for MALORY that failed to disclose the true address for MALORY.
- B. Respondent MALORY, by and through respondents STEIN, STRAUSS, ZELMER, ZARINEGAR, CGI, WILSON, and FENN, filed false financial statements that incorrectly identified underwriting fees as commissions earned.

127. By virtue of the foregoing, Respondents violated Sections 12.F, 12.G, and 12.E of the Act.

#### **GROUND FOR REVOCATION**

128. Section 8.E(1)(b) states, *inter alia*, that the registration of a salesperson or dealer may be revoked if the Secretary of State finds that the salesperson has engaged in any unethical practice in connection with any security, the offer or sale of securities, or in any fraudulent business practice. Respondents MALORY and STEIN are subject to revocation pursuant to Section 8.E(1)(b) of the Act, in that:

- A. Respondents MALORY, STEIN, STRAUSS, ZELLMER, CGI, WILSON and FENN filed a Broker-Dealer application for MALORY that failed to disclose the true address for MALORY.
  - B. Respondents MALORY, STEIN, STRAUSS, ZELLMER, ZELLMER, CGI, WILSON and FENN allowed Respondent WILSON to act as an undisclosed principal of MALORY, despite the fact his prior felony conviction for securities fraud barred him from any association with a Broker-Dealer.
  - C. Respondents MALORY, STEIN, STRAUSS, ZELLMER, ZELLMER, CGI, WILSON and FENN filed a Broker-Dealer application for Malory Investments that failed to disclose Respondent WILSON'S involvement in MALORY.
  - D. Respondents MALORY and STRAUSS filed a false U4 application in that the application failed to disclose STRAUSS' prior criminal convictions.
  - E. Respondents MALORY and STRAUSS filed a false U4 application in that the application failed to disclose that STRAUSS and Stovact were subject to a Desist and Refrain Order issued by the State of California. STRAUSS' U4 application also failed to disclose that STRAUSS was acting as the Chief Operating Officer of Stovact Inc. at the time of that Desist and Refrain Order.
  - F. Respondent MALORY, by and through Respondents STEIN, STRAUSS, ZELLMER, ZELLMER, CGI, WILSON and FENN, filed false financial statements that incorrectly identified underwriting fees as commissions earned.
  - G. Respondents CGI, WILSON and FENN held CGI out to the public as a Broker-Dealer, while CGI was not registered as such.
  - H. Respondents CGI, WILSON and FENN offered their clients a list that disclosed the covert names and telephone numbers used by the FBI and state securities regulators.
  - I. Respondents MALORY, STEIN, STRAUSS, ZELLMER, ZELLMER, CGI, WILSON, and FENN filed notice filings with the Illinois Securities Department which claimed that Respondent MALORY was an associated Broker/Dealer of the offering, when MALORY failed to conduct any due diligence.
129. Section 8.E(1)(e) states, *inter alia*, that the registration of a salesperson or dealer may be revoked if the Secretary of State finds that the salesperson or dealer has (i) failed reasonably to supervise the securities activities of any of its salespersons or other employees and the failure has permitted or facilitated a violation of Section 12 of the Act, or (ii) is offering or selling or has offered or sold securities in this state through a

salesperson other than a registered salesperson, or in the case of a salesperson is selling or has sold securities in this state for a dealer with knowledge that the dealer has not complied with the provisions of this Act or (iii) has failed reasonably to supervise the implementation of compliance measures following notice by the Secretary of State of noncompliance with the Act or with the regulations promulgated thereunder or both or (iv) has failed to maintain and enforce written procedures to supervise the types of business in which it engages and to supervise the activities of its salespersons that are reasonably designed to achieve compliance with applicable securities laws and regulations. MALORY and STEIN are subject to revocation pursuant to Section 8.E(1)(e) of the Act, in that they:

- A. allowed WILSON to act as an undisclosed principal of MALORY, despite the fact that as a result of his earlier securities fraud conviction, WILSON was barred from any association with a Broker-Dealer.
- B. failed to have any written policies relating to anti-money laundering procedures.
- C. failed to have any procedures for reviewing correspondence.
- D. failed to maintain incoming and outgoing correspondence.
- E. failed to have any system to archive e-mail relating to the operation of MALORY.
- F. failed to maintain client account records.
- G. registered offerings as a Broker-Dealer of record, without conducting any due diligence.
- H. allowed WILSON and FENN, neither of whom was registered with MALORY, to negotiate underwriting agreements on behalf of MALORY.
- I. failed to conduct background investigations on new employees, as required by their own supervision procedures.
- J. allowed WILSON and FENN to hire new agents on behalf of MALORY, despite WILSON and FENN not being registered with MALORY.
- K. allowed WILSON and FENN to make regulatory and registration filings on behalf of MALORY, with little or no review by a designated Principal.

- L. failed to conduct compliance reviews of its branch offices, as required by their own supervision procedures.
  - M. failed to conduct a pre-employment interview prior to registering Kirk Devon Smith.
  - N. failed to conduct any inquiry into the activities of Kirk Devon Smith, after his previous employer was named in a SEC enforcement case.
  - O. failed to conduct any inquiry into the activities of fourteen (14) agents that had dual registration with MALORY and North American Resources, after North American Resources was named in an Alabama Cease and Desist Order.
  - P. failed to conduct a due diligence review in any of the offerings for which it acted as the associated Broker-Dealer.
  - Q. failed to conduct reasonable review to confirm that the Private Placement Memoranda associated with the offerings disclosed the principals' prior criminal convictions.
  - R. failed to conduct reasonable review to confirm that the Private Placement Memoranda did not contain false or misleading statements.
  - S. failed to conduct reasonable review to confirm that the offerings were sold in a manner consistent with exemptions claimed in the Private Placement Memoranda.
130. Section 8.E(1)(q) of the Act states, *inter alia*, that the registration of a Salesperson may be revoked if the Secretary of State finds that the Salesperson has failed to maintain the books and records required under the Act or rules or regulations promulgated under the Act or under any requirements established by the Securities and Exchange Commission or a self-regulatory organization. MALORY and STEIN are subject to revocation pursuant to Section 8.E(1)(q) of the Act, in that they:
- A. failed to produce and/or maintain accurate financial statements.
  - B. failed to produce and/or maintain financial records including check books, bank statements, cancelled checks and cash reconciliations.
  - C. failed to produce and/or maintain incoming and outgoing correspondence, including e-mail.



- D. failed to have any system to archive e-mail relating to the operation of MALORY.
  - E. failed to produce and/or maintain client files.
  - F. failed to produce and/or maintain employment records for certain registered representatives.
  - G. failed to produce and/or maintain records in regard to disciplinary actions against registered representatives registered with MALORY.
  - H. failed to produce and/or maintain due diligence files relating to its underwriting clients.
  - I. failed to produce and/or maintain notice filings filed on behalf of its underwriting clients.
  - J. failed to produce and/or maintain subscription agreements, indications of interest, escrow agreements, banks records, sales blotters, and certain Broker-Dealer agreements for transactions relating to the sale of the securities of its underwriting clients.
131. Section 8.E(1)(g) of the Act states, *inter alia*, that the registration of a Salesperson may be revoked if the Secretary of State finds that the Salesperson has violated any provisions of the Act.
132. Section 8.E(3) of the Act provides, *inter alia*, that the Secretary of State may institute a revocation proceeding within two years one year after withdrawal became effective and enter a revocation order as of the last date on which registration was effective.
133. By virtue of the foregoing, the Broker-Dealer and Salesperson registrations of Respondents MALORY and STEIN in the State of Illinois are subject to revocation as of the last date on which registration was effective, pursuant to Section 8.E(1)(b), 8.E(1)(e), 8.E(1)(q), 8.E(1)(g) and 8.E(3) of the Act.


You are further notified that you are required pursuant to Section 130.1104 of the Rules and Regulations (14 Ill. Adm. Code 130)(the “Rules”), to file an answer, special appearance, or other responsive pleadings to the allegations above within thirty (30) days of the receipt of this

Notice. A failure to file an answer within the prescribed time shall be construed as an admission of the allegations contained in the Notice of Hearing.

Furthermore, you may be represented by legal counsel; may present evidence; may cross-examine witnesses and otherwise participate. A failure to appear shall constitute a default by you.

Delivery of Notice to the designated representative of the Respondent constitutes service upon such Respondent.

Dated: This 6th day of July, 2007.

  
JESSE WHITE  
Secretary of State  
State of Illinois

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